



State and Local Tax Update

Chris Oatis and Brian Howsare

November 12, 2024

Chris Oatis

Principal, Grant Thornton Advisors

- Florida CPA based in Orlando focused on state tax compliance and consulting
- Board of Directors member and former Committee Chair, FICPA
- Regular presenter for COST, FICPA, and other tax/accounting seminars
- Studied mental health counseling before becoming an accountant

Brian Howsare

Senior Manager, Grant Thornton Advisors

- Florida attorney based in Tampa focused on tax controversy and consulting
- Former Division Assistant Director, Tax Section of the Florida Bar
- Publications in Pittsburgh Tax Review, Bloomberg BNA, and Tax Notes
- Gold medal winner – Best Florida Beer Homebrew Competition

Objectives

Upon completion of this session, attendees will have a better understanding of the most consequential state income and indirect tax law changes resulting from recent legislative and rulemaking efforts, as well as state tax jurisprudence. Attendees will also have an increased understanding of changes in jurisdictions' positions and policy as stated in advisements and bulletins issued by tax authorities.

Agenda

- State income tax updates impacting the current and upcoming tax years
- A look at recent developments in pass-through entity tax developments and states' positions on P.L. 86-272
- State indirect tax updates

The slide features four horizontal orange lines of varying lengths and positions. The top line starts with a dot on the left and extends across the top. The second line starts from the left edge and ends with a dot on the right. The third line starts with a dot on the left and extends across the middle. The bottom line starts from the left edge and ends with a dot on the right.

State Income Tax Reform

State Tax Reform

Audience Poll – Show of Hands

The 2023 and 2024 state legislative sessions for income and sales tax can be best described as:

- A) Snooze-fest. Nothing impactful for me.
- B) Mild. Worth following but nothing too impactful happening
- C) Somewhat spicy. A few fairly impactful changes that may portend some difficulty down the road.
- D) Ay chihuahua! It's going to be difficult to keep up with the changes!

State Tax Reform

Arkansas

- Reduced highest corporate income tax rate from 4.8% to 4.3%

Connecticut

- NOL carryover period increases from 20 to 30 years starting Jan. 1, 2025
- Allows certain combined groups to deduct, over a 30-year period, the amount necessary to offset the increase in the valuation allowance against NOLs and tax credits in Connecticut that resulted from the State's shift to combined reporting.

Colorado

- Corporate income tax rate decrease from 4.40% to 4.25% for 2024 tax year
- Lowered combined reporting requirements – Members of an affiliated group of C-corporations that are members of a unitary business must file as a combined group starting Jan. 1, 2026 (previously combined reporting only required if 3/6 specific unitary test were met over three successive years).

State Tax Reform

California

- NOL deductions suspended for taxpayers with income over \$1m for 2024, 2025, and 2026 tax years; NOL carryover period extended for each year of disallowance.
- Limitation on credits – Max. tax reduction from corporate credits, including carryover, is \$5m for 2024, 2025, and 2026
- Above limitations will not apply if Director of Finance determines general funds are sufficient.
- Irrevocable election available to receive an annual refundable credit equal to 20% of the credits that would be available but for the \$5m credit limitation; Begins the third taxable year after the election is made.
- Codifies Ruling 2006-01 – Transaction or activity that is not included in “net income” is not included in apportionment factor; Suspends procedural rulemaking requirements for this provision

State Tax Reform

California – The *Microsoft Case* and SB 167

Issue: Whether Microsoft can include the gross amount of its repatriated dividends in the denominator of its sales factor before applying the 75% qualifying dividend deduction.

- Legal Ruling 2006-01 – FTB determined that the sales factor includes only net dividends after applying the qualifying dividend deduction.
- July 2023 – Office of Tax Appeals (OTA) holds that Microsoft could include gross receipts in its sales factor.
 - Specifically declined to follow FTB’s longstanding position from Rul. 2006-01. No deference given to FTB’s interpretation because the ruling is not a regulation, and it is an interpretation of a statute, not a FTB reg.
 - Rejected alternative apportionment argument
- Feb. 2024 – OTA denied FTB Petition for Rehearing
 - Consistent with Southern Minn. Beet Sugar Coop.

State Tax Reform

California – The *Microsoft* Case and SB 167

- SB 167 – Overrules OTA’s *Microsoft* decision
 - For taxable years beginning on or after June 27, 2024, Legal Ruling 2006-01 applies to apportionment factors attributable to corporate taxpayers.
 - To the extent a transaction or activity generates income or loss not included in net income subject to apportionment, it is excluded from the apportionment formula.
- SB 167 – Weight of authority for regulations and sub-regulatory guidance from FTB
 - FTB may adopt regs necessary to further the purpose of this law (preventing deductible income from being included in apportionment construction)
 - The Administrative Procedures Act does not apply to any regulation or sub regulatory guidance issued under this law.

State Tax Reform

Florida

- Automatic extension for CIT taxpayers if federal income tax return is extended due to a federally declared disaster in the state (15 days after federal income tax due date)

Georgia

- Corporate income tax rate imposed at the same rate as individual income tax starting Jan. 1, 2024; Individual income tax rate set to decrease by 0.1% annually until it is 4.99% (from 5.39%)

Illinois

- NOL deductions limited to three years
- For taxable years ending on or after December 31, 2024, and prior to December 31, 2027, the maximum amount of an NOL that a C Corporation may deduct is limited to \$500,000 (previously \$100,000).
- Financial organizations' Investment income sourced based on a ratio of non-investment income sourcing, not on fixed place of business.

State Tax Reform

Indiana

- Continues to allow expensing for IRC § 174 R&E expenses

Kentucky

- Deduction for combined reporting delayed – 10% offset available to taxpayers suffering an adverse impact from shifting from separate to combined reporting is delayed to the start of Jan. 1, 2026 (from Jan. 1, 2024)

Louisiana

- Extensions – 6-month extension now automatic for partnerships and S-corps whose federal due date is after the Louisiana due date.
- Corporate extension reduced from 7 months to 6 months

Noteworthy Rulings

Maine

- Service receipts sourced to location of customer's customer – Receipt of services of prescription benefit management services is where individuals fill their prescriptions at retail pharmacies, not where the customer (insurer or employer) is.

Massachusetts

- Business corporations and financial institutions must apportion using only the sales factor starting Jan. 1, 2025.

Minnesota

- Income is apportionable business income unless it is nonbusiness income – Sale of an S-corp's goodwill was not "nonbusiness income." Therefore it is apportionable.
- Preparation of market research reports by sales reps in Minnesota exceed "solicitation of orders" for P.L. 86-272.

State Tax Reform

Nebraska

- Qualifying property under IRC § 168 is eligible for full expensing under IRC § 168 if the cost was not deducted in determining federal taxable income starting Jan. 1, 2025.
- Research or experimental expenditures may be deducted instead of capitalized if not deducted in calculating federal taxable income starting Jan. 1, 2025

New Jersey

- 2.5% Corporate Transit Fee surtax on certain NJ CBT taxpayers with taxable net income over \$10m starting Jan. 1. 2024
- For privilege periods ending on/after July 31, 2023:
 - NJ adopts IRC § 172(a)(2) NOL limitation under but substitutes the dates provided in the section. As a result, an 80% limitation applies; New rules for members of combined groups
 - State can adjust NOLs in out-of-statute periods to assess for a period in statute

Poll Break

Pop culture: Guess the year!

- Top selling album of the year is Taylor Swift's "1989"
- Deflategate dominates sports talk
- Societal divide over "the dress"
- Hottest new celebrity is Left Shark
- New York tax regulations formally adopted in Dec. 2023 are effective beginning Jan. 1 of this tax year.

Is the year:

a) 2015

b) 2018

c) 2021

D) 2024



State Tax Reform

New York Administrative Rule Adoption – Noteworthy Items

- Apportionment
 - TPP sales – Location of customer
 - Services and other receipts – Where customer receives benefit
 - Intangible assets – Where activities relating to intangibles are performed
 - Digital products – Primary use with business address presumption
 - Others – Sale of partnership interest, installment sales, lump sum payments
- Economic nexus standard – \$1m in receipts
- Alternative apportionment – Written request required
- Retroactive Application?
- P.L. 86-272 – Alignment with 2021 MTC statement – first state to codify in regs.

State Tax Reform

Pennsylvania

- Net loss cap of 40% post-apportionment income increased by 10% annually to align with federal 80% limitation by 2029 tax year
- For net losses incurred in 2025 and after, taxpayer applies the actual percentage for the tax year and subtracts the actual percentage of taxable income deducted from pre-2025 net losses

Rhode Island

- NOL carryover period increases from 5 to 20 years starting Jan. 1, 2025.
- Banking institutions may use single sales factor apportionment starting Jan. 1, 2025.

Four horizontal orange lines of varying lengths are arranged in a staggered pattern. Each line has a solid orange circle at its end. The top line is the longest and is positioned highest. The second line is shorter and positioned lower. The third line is the shortest and positioned lowest. The fourth line is the same length as the second line and is positioned between the second and third lines.

PTE Updates

PTE Updates

PTE Tax Background

Tax Cuts and Jobs Act (TCJA) imposed a limit on the amount of state and local taxes that individuals may deduct for federal income tax purposes

- Beginning with the 2018 tax year, most individuals and married couples filing a joint return are now limited to a \$10,000 annual SALT deduction
- States have enacted laws in response to the \$10,000 SALT deduction cap that create an entity-level tax on pass-through entities (PTEs) and provide owners either a corresponding individual tax credit or an exclusion from tax for the individual's pass-through income
- The IRS released guidance on Nov. 9, 2020 agreeing that PTEs can claim an entity-level deduction for state tax paid under state laws that shift the tax burden from individual owners to the business entity (Notice 2020-75)

PTE Updates

PTE Tax Background

- End of 2020: Seven PTE tax regimes existed
- End of 2021: After release of Notice 2020-75, 15 additional states moved at a rapid pace to adopt their own elective PTE regimes. Why?
 - Notice 2020-75 provided acceptable framework for PTEs to deduct tax at the entity level
 - For the states, a workaround of the federal SALT cap is generally a revenue-neutral mechanism to provide relief to individual taxpayers in high-tax and low-tax states alike
- Now 37 states with PTE taxes

PTE Updates

2024 Changes

- Alabama – Extended due date for making PTE election
 - 2024 – on or before filing deadline; 2025 – on the timely filed return + extensions
- Hawaii – Rate is 9% of qualified members' distributive shares plus guaranteed payments of HI taxable income (formerly 11%, the highest individual income tax rate)
- Kansas – Tax now imposed at the highest individual income tax rate for the tax year (previously 5.7%)
- Missouri – Option to calculate tax using state business income deduction instead of federal
- Oklahoma – Extended for election – Now allows election on timely filed return + extension
- Rhode Island – Reduces credit to 90% of the tax paid by the PTE at the entity level (from 100%)
- West Virginia – Promulgated rules to implement the elective PTE



P.L. 86-272 Updates

PL. 86-272 Updates

PL. 86-272 Background

- 1959 Federal Law
 - Prohibits a state from imposing a net income tax on the income of a business derived from within a state through interstate commerce if its only business activities within the state consist of the solicitation of orders from sales of tangible personal property (TPP).
 - No updates by Congress to address applying 86-272 the modern economy/electronic commerce.
- 2021 MTC Statement –
 - Revised statement interpreting 86-272 as applied to modern economy and online business activities
 - Provides 11 examples of different activities conducted by internet businesses and whether they are protected by 86-272

P.L. 86-272 Updates

P.L. 86-272 Recent State Guidance

- Multiple jurisdictions have issued guidance adopting the MTC's interpretation of P.L. 86-272, including:
 - Minnesota – Minn. Draft Revenue Notice (Apr. 2023)
 - New Jersey – N.J. Technical Bulletin TB-108 (Sept. 2023)
 - N.Y. Regulations – tit. 20 § 1-2.10 (Dec. 2023)
 - California – TAM 2022-10

P.L. 86-272 Updates

PL. 86-272 – TAM 2022-10 and *American Catalog Mailers Ass'n. v. Franchise Tax Board*

- California FTB TAM 2022-10 – Explains FTB’s position on the application of P.L. 86-272 protection in the modern economy
 - Does not explicitly adopt the revised MTC statement, but is generally consistent with the positions in the MTC’s statement
 - Addresses the same 11 internet activities that are outlined in the MTC’s statement and reaches the same conclusions
 - TAM does not contain any effective date or limiting principle regarding how it may be applied by the FTB in auditing prior years
- ACMA challenged the TAM as an unpromulgated rule under the Administrative Procedures Act (APA) – Superior Court for San Francisco County agreed
 - Issue: is the TAM a regulation for purposes of the APA?
 - Tidewater test determines

The slide features three horizontal orange lines. The top line starts with a solid orange dot on the left and extends across the top. The middle line starts from the left edge and ends with a solid orange dot on the right. The bottom line starts from the left edge and ends with a solid orange dot on the right. The text 'Indirect Tax Updates' is centered between the middle and bottom lines.

Indirect Tax Updates

Indirect Tax Updates

Travel Companies

- Florida Enacts Tax Collection Requirements for Vacation Rental Advertising Platforms
- Alabama requires “accommodations intermediaries” to collect state lodging taxes as of Jan. 1, 2025.
- Illinois Considers Online Travel Companies as Hotel Operators Responsible for Collecting the Hotel Operators’ Occupation Tax.
- Vermont Enacts a Short-term Rental Surcharge
- Louisiana: Online travel booking companies not required to collect tax on their markup – *Robinson v. Priceline*

Indirect Tax Updates

Groceries

- Illinois – 1% tax on groceries repealed Jan. 1, 2026; localities authorized to impose their own 1% tax
- Oklahoma – 0% rate for groceries
- Tennessee – Localities allowed to impose a lower rate for groceries than for other taxable sales
- Pennsylvania: Carbonated water taxable as a soft drink – *Montgomery v. Pennsylvania*

Indirect Tax Updates

Leases

- Illinois – Sales of property to be leased exempt as sale for resale; Lease streams taxable Jan. 1, 2025
- Maine – Lease streams now taxable; Purchase of TPP to be leased is nontaxable; Refund available for lessors that bought lease property between Jan. 1, 2023 and Jan. 1, 2025.

Potpouri

- Colorado – Excise tax on firearms and ammunition enacted
- Colorado – Home rule localities not using SUTS may not collect from retailers without physical presence
- Kentucky – Imposition on numerous services
- Oklahoma – Exemption for digital asset mining equipment and electricity
- Vermont – Repeal of SaaS exemption
- Washington – Admin rule confirms look-through to customer's market

Indirect Tax Updates

Florida Focus

- Communications Services Tax – Offerings with digital video component
 - Reversal of prior advisements
 - No true object/predominant purpose test
- Increase of sales tax holidays
 - Disaster preparedness
 - Freedom month
 - Tool time
 - Back to school

Indirect Tax Update

Chicago Settlement of “Netflix Tax” with Apple

- City’s tax on amusements includes “any paid television programming” at 9%
- Chicago estimated assessment of at least \$13m based on remittances by Apple competitors Disney+ and Spotify
- Prior challenges to the tax on behalf of Hulu, Netflix, and Spotify were defeated at appellate court level.
- Apple’s lawsuit asserted Chicago’s tax violated the commerce and due process clauses of the U.S. Constitution, and the Internet Tax Freedom Act (ITFA), which bars states and localities from imposing discriminatory taxes on electronic commerce.
- Apple’s suit was dismissed by a circuit court judge in March 2022.
- Settled for \$0 in back taxes and an agreement to collect prospectively from Sept. 2022.



Thank You

Brian Howsare and Chris Oatis